Congress of the United States
Washington, DC 20515

July 31, 2023

The Honorable Jerome H. Powell
Chair
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

The Honorable Martin J. Gruenberg
Chairman
Federal Deposit Investment Corporation
550 17th St. NW
Washington, DC 20429

The Honorable Todd M. Harper
Chairman
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314

The Honorable Michael J. Hsu
Acting Comptroller of the Currency
Office of the Comptroller of the Currency
400 7th St. SW
Washington, DC 20219

Dear Chairman Powell, Chairman Gruenberg, Chair Harper, and Acting Comptroller Hsu,

We write to request information on how your agencies are assessing and responding to the challenges facing the operation and regulation of the commercial real estate (CRE) lending in light of the disruption and instability caused by the COVID-19 pandemic, and the unique challenges facing regional banks. We are especially interested in the impact of this instability on the $6 trillion dollar market for retail and office space CRE, which has been unduly impacted by pandemic related disruptions.

As you are no doubt deeply aware, the short-term shock to and long-term reorientation of the commercial real estate industry caused by the COVID-19 pandemic forced millions of businesses to rapidly transition their labor force to remote work, their interactions with consumers to virtual platforms, and the sale of their goods and services to online sales. Combined with temporary steep reduction in revenues, aggressive layoffs and other sudden shocks, many commercial tenants have found it convenient, economical, or necessary to reduce their costs and physical footprint by either cancelling or declining to renew their leases.

We have observed that this realignment of commercial tenant priorities has led to a marked decline in commercial tenancy rates across the country, a reality which has continued past the end of the public health emergency as businesses continue to adjust their operations to a fundamentally changed economy. The resulting sudden and unexpected loss of significant rent for commercial real estate owners is causing a significant number of owners to be unable to pay back their loans, many of which had their terms set before the pandemic or before the long term impacts the pandemic would have on the economy and demand became clear.

This is especially important when the impacts of a destabilized commercial real estate sector are likely to influence future lending, economic growth and especially the health of commercial centers and mixed-use neighborhoods. **As our cities and neighborhoods continue to face soaring rents, rising rates of homelessness, and a severe lack of affordable, high-quality housing, it is essential that all arms of the federal government take prudent steps to limit the impact of a CRE market contraction, and innovate to encourage reuse of vacant commercial space as a potential source of housing.**

Over the past months, we have closely followed reports and data indicating instability in the CRE market and its potential effects on the financial system. Trepp, an industry analysis firm, has reported that over $250 billion dollars of CRE bank loans are scheduled to be due in 2023.

Analysis from the Mortgage Bankers Association indicates substantial increases in measures of mortgage delinquency rates measured across the industry. MBA analysis also indicates that of the approximately $750 billion of outstanding office space CRE debt (roughly 30% of the non-multifamily CRE debt market), $339 billion, or roughly 45% of that amount, is held by banks directly on their balance books, with around $98 billion of that debt scheduled to be due in 2023.

We find these statistics concerning when data indicate that CRE investments make up a significantly larger proportion of regional banks assets', compared to their larger competitors. JPMorgan Private Bank estimates that smaller banks have 4.4 times more exposure with CRE loans, which make up 28.7% of assets compared to 6.5% at larger institutions. JP Morgan concludes with an expectation that an alarming 21% of office CRE loans contained in mortgage-backed securities will eventually default.

These indicators are even more concerning, when evaluated in the context of the direct exposure of American financial institutions in the CRE market. Analysis from Trepp last month of publicly disclosed regulatory data, indicates that more than 15% of 4760 banks have CRE or construction loan concentrations that exceed thresholds set by FDIC for greater regulatory scrutiny, which for CRE loans is a ratio exceeding 300% of total capital, with an even higher proportion of smaller regional banks exceeding the threshold.

Given the recent collapse of multiple regional banks due to factors including decreases in consumer confidence, rising interest rates, poor internal risk assessment, a lack of sufficient of diversification of assets, and acknowledged failures in proactive regulatory action, we consider it prudent to thoroughly investigate another potential rising risk factor for regional banks, and the larger financial system.

As lawmakers ultimately responsible for and setting federal policy for the oversight and regulation of our financial sector and the mitigation of financial risk to our larger economy, we believe that clarity and additional information is required from your agencies to guide our next steps, and request your response to the following areas of inquiry:

1. Given current market conditions in the wake of the pandemic, do your agencies assess greater than normal risk in the commercial real estate market in the near and long term?
2. Do you assess higher levels of risk for regional/small banks as compared to their larger competitors?
3. Given potential instability in the CRE market, what supervisory actions have been or are being taken/developed by your agencies to account for this potential increased risk?
4. Given the declining demand for office CRE leases, and consistent increase in demand for housing, including multi-family housing CRE leases, are your agencies aware of and/or recommending any specific mechanisms to stabilize the CRE market by incentivizing conversions of unused, underperforming office CRE to affordable housing?
5. Can you detail how your recent June 29th updated interagency policy statement on prudent commercial real estate loan accommodations and workouts has taken into account the unprecedented disruptions of the COVID-19 pandemic and the current instability in the CRE loan market?
    a. How have the changes to the CRE lending market from 2020 onwards directly affected the changes and clarifications in the updated statement?
    b. Do your agencies believe the recent updates to the statement/guidance are sufficient to address the developing issues in the CRE market for the foreseeable future?
6. To our knowledge, publicly available regulatory data does not consistently distinguish the specific sectors of commercial real estate that reported commercial real estate loans are invested in (e.g., office space, multi-family housing, retail, etc.).

   a. Do your agencies have access to more specific commercial loan data broken-down for specific CRE sectors in order to assess the risks involved in asset portfolios?
   b. If this data is available to regulators, would it be possible to publish these breakdowns by sector in public data?
7. Are your agencies able to confidently assess what proportion of CRE loans are being issued to institutional versus smaller commercial owners?
8. Do your agencies plan to publish public reports that approximate the near-term potential impacts of CRE market stress, particularly within the office and retail space, on the banking system?
9. Do your agencies plan to issue any publications on the effects of the long-term realignment of the commercial real estate sector, and the need/potential mechanisms to diversify CRE holdings away from potentially unstable sectors towards potentially more stable revenue streams such as mixed-use and multifamily commercial real estate?
10. What additional legislative actions do your agencies recommend Congress take to diversify and stabilize the CRE market, improve the utilization, profitability, and economic value of unused commercial space, and reduce negative pressure on local economies, as well as large and regional banks?

Thank you for your time and consideration of our inquiries and look forward to your responses.

Sincerely,

Jimmy Gomez
Member of Congress

John B. Larson
Member of Congress

Daniel T. Kildee
Member of Congress

Donald S. Beyer Jr.
Member of Congress

Ilhan Omar
Member of Congress

Summer Lee
Member of Congress

Jasmine Crockett
Member of Congress

Barbara Lee
Member of Congress

Maxwell Alejandro Frost
Member of Congress

Greg Casar
Member of Congress

CC: Secretary Janet Yellen
Secretary Marcia Fudge